

WATER/ICRJ/RHG

Decision \_\_\_\_\_

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF  
CALIFORNIA**

In the Matter of the Application of SUBURBAN  
WATER SYSTEMS U-391-W for Authority to  
issue, sell, and deliver its Series D First Mortgage  
Bonds not exceeding \$15,000,000 principal  
amount.

Application 04-02-012  
(Filed February 18, 2004)

**OPINION GRANTING AUTHORITY TO ISSUE DEBT SECURITIES**

**Summary**

This decision grants Suburban Water Systems (Suburban) the authority requested in Application (A.) 04-02-012 (Application).

Suburban requests authority, pursuant to §§ 816, 817, and 851 of the California Public Utilities (Pub. Util.) Code and Rules 33 and 34 of the Commission's Rules of Practice and Procedure to issue, sell and deliver for cash up to \$15,000,000 Series D First Mortgage Bonds due 2024 (Series D Bonds). Suburban also seeks exemption from the Commission's Competitive Bidding Rule in relation to the proposed Series D Bonds.

Notice of the filing appeared on the Commission's Daily Calendar of February 23, 2004. No protests have been received.

**Background**

Suburban is a California public utility corporation engaged in the business of providing water service to an area covering approximately 43

square miles in Orange and Los Angeles counties, comprising all or part of Glendora, Covina, West Covina, Walnut, La Puente, Hacienda Heights, City of Industry, Whittier, La Mirada, La Habra, Buena Park, and other unincorporated areas. Suburban is a wholly owned subsidiary of Southwest Water Company.

## **Discussion**

Suburban seeks authorization to obtain debt capital in an aggregate principal amount not to exceed \$15,000,000 through the issuance and sale of the Series D Bonds.

Suburban has not, at the present time, entered into any contract for the purchase and sale of the Series D Bonds but plans to place them privately with one or more institutional investors. Because of changing market conditions, Suburban requests Commission authority to offer, issue and deliver the Series D Bonds with interest rates based on market conditions existing at the time of negotiating the terms.

## **Series D First Mortgage Bonds**

In 1980, Suburban issued \$15,000,000<sup>1</sup> of 8.93% Series A First Mortgage Bonds due 2006 pursuant to an Indenture of Mortgage and Deed of Trust (Mortgage Indenture) of which \$3,300,000 is still outstanding.

In 1992, Suburban issued \$8,000,000<sup>2</sup> of 9.09% Series B First Mortgage Bonds due 2022 pursuant to a Second Amendment and Supplement to the Mortgage Indenture of which \$8,000,000 is still outstanding.

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<sup>1</sup> Authorized by Decision (D.) 86-11-013.

<sup>2</sup> Authorized by D.92-01-026.

In 1996, Suburban issued \$8,000,000<sup>3</sup> of 7.61% Series C First Mortgage Bonds due 2006 pursuant to a Third Amendment and Supplement to the Mortgage Indenture of which \$8,000,000 is still outstanding.

The Series D Bonds will represent the fourth series of First Mortgage Bonds issued by Suburban. They will be direct obligations of Suburban and will rank *pari passu* with other First Mortgage Bonds of Suburban issued under the Indenture. The interest payments will be semi-annual.

The Series D Bonds are redeemable prior to maturity, in whole or in part, (a) at the option of Suburban at any time on not more than sixty and not less than thirty days prior notice, at par plus accrued interest, plus the Make-Whole Amount<sup>4</sup>, if any, and (b) upon receipt of proceeds equal to or exceeding \$15,000,000 by the trustee under the Indenture as a result of a casualty or condemnation, at the option of Suburban at par plus accrued interest, without the Make-Whole Amount.

Suburban states in the Application that the Bond Purchase Agreement will contain provisions similar to the Bond Purchase Agreement dated as of October 21, 1996 between Suburban and the Purchaser named therein for the Company's 7.61% Series C First Mortgage Bonds. The Bond Purchase Agreement will also include appropriate modernization adjustments<sup>5</sup> in Private Placement Enhancement Project Model Form No. 2 (Model Form) and other appropriate provisions for the Series D Bonds.

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<sup>3</sup> Authorized by D.96-10-032.

<sup>4</sup> The excess amount of the discounted value of the remaining scheduled payments for the principal called for redemption over the amount of such called principal. The Make-Whole Amount may in no event be less than zero. For purposes of the discounted value, the rate is equal to the interpolated yield of a U.S. Treasury security with maturity equal to the remaining life of the called bonds plus 50 basis points.

<sup>5</sup> Changes in law or practice.

The Fourth Amendment and Supplement to Suburban's existing Indenture of Mortgage and Deed of Trust will contain similar provisions to the provisions contained in the Third Amendment and Supplement to Indenture dated October 9, 1996 pursuant to which the Series C Bonds of the Company were issued, with some modernization adjustments from the Model Form and other appropriate provisions for the issuance of the Series D Bonds.

### **Use of Proceeds**

Suburban intends to apply the net proceeds from the proposed issue of the Series D Bonds: (i) to refinance \$3,300,000 of Suburban's outstanding 8.93% First Mortgage Bonds, Series A and (ii) to finance a portion of Suburban's capital expenditure program from 2004 through 2008.

We will authorize Suburban's proposed issue of Series D Bonds in the aggregate principal amount of \$15,000,000.

Pub. Util. Code § 817(b) allows a public to issue stocks or evidences of indebtedness payable at a period of more than 12 months for the construction, completion, extension, or improvement of its facilities. Also, Pub. Util. Code § 817(d) allows a public utility to issue stock or evidences of indebtedness payable at a period of more than 12 months for the discharge or lawful refunding of its obligations.

Pub. Util. Code § 1904(b) states that no fee need be paid on such portion of any such issue as may be used to guarantee, take over, refund, discharge, or retire any stock, bond, note or other evidence of indebtedness on which a fee has been paid to the Commission.

Pursuant to Pub. Util. Code § 818, we will approve Suburban's proposed issue of Series D Bonds, the proceeds of which are to be used to refinance existing long-term debt and for capital expenditures.

Pursuant to Pub. Util. Code § 851, we will allow Suburban to encumber its property whenever such encumbrance serves to secure the debt authorized herein.

We place Suburban on notice that the reasonableness of any resulting interest rate and cost of money arising from debt capital are normally subject to review in cost of capital or general rate case proceedings.

### **Competitive Bidding Rule**

Under the provisions of Resolution No. F-616, Suburban's proposed issue and sale of Series D Bonds is exempt from the Commission's Competitive Bidding Rule because the principal amount does not exceed \$20,000,000.

**Financial Information**

For the nine months ending September 30, 2003, Suburban reported total operating revenues of \$32,374,000 and net income of \$4,432,000, as shown in its Consolidated Statement of Income and Retained Earnings, attached as Exhibit B to the Application. Suburban's Consolidated Balance Sheet at September 30, 2003, shown also as part of Exhibit B, is summarized as follows:

(dollars in thousands)

<u>Assets</u>	<u>Amount</u>
Net Property, Plant and Equipment	\$ 86,169
Current Assets	8,439
Other Assets	<u>3,674</u>
Total Assets	<u>\$ 98,282</u>
<u>Capitalization and Liabilities</u>	
Cumulative Preferred Shares	\$ 3,982
Common Shares	745
Paid In Capital	5,017
Retained Earnings	<u>31,526</u>
Total Stockholders' Equity	\$ 41,270
Current Liabilities	\$ 7,368
Long-Term Debt	19,300
Advances for Construction	5,256
Deferred Income Taxes	9,171
Contributions in Aid of Construction	6,978
Other Liabilities	<u>8,939</u>
Total Liabilities	\$ 57,012
Total Capitalization and Liabilities	<u>\$ 98,282</u>

Construction Budget

Suburban's projected construction budgets for 2004 through 2008, as shown in Exhibit E to the Application, are as follows:

<u>Components</u>	(dollars in thousands)				
	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
New Wells and Supply	1,052	0	0	1,000	1,000
Reservoir Improvements	2,877	1,275	1,505	2,566	750
Pumps and Equipment	110	2,000	4,630	2,700	700
Replace Transmission Mains	302	0	0	0	0
New Transmission Mains	693	992	300	0	1,300
Distribution Main					
Replacements	677	0	300	214	530
Other	<u>1,630</u>	<u>1,233</u>	<u>1,265</u>	<u>1,220</u>	<u>1,220</u>
Total	<u>\$7,341</u>	<u>\$5,500</u>	<u>\$8,000</u>	<u>\$7,700</u>	<u>\$5,500</u>

We will not make a finding in this decision on the reasonableness of Suburban's proposed construction program. Construction expenditures and the resulting plant balances in rate base are issues that are normally addressed in general rate cases.

Projected Cash Requirements

Suburban's estimate of cash requirements for 2003 through 2005 is summarized as follows:

<u>Components</u>	(dollars in thousands)				
	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
Construction Expenditure	7,341	5,500	8,000	7,700	5,500
Repayment of Series A Bonds	<u>3,300</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Subtotal	10,641	5,500	8,000	7,700	5,500
Less: Estimated Cash Provided from Internal Sources and Short Term Borrowing	(4,180)	(4,195)	(4,408)	(4,701)	(4,914)
External funding required	6,461	1,305	3,592	2,999	586
% of Available Cash to Needed Funds	39%	76%	55%	61%	89%

Suburban's projected cash requirements indicates that internally generated funds will provide approximately \$22,398,000 or 60% of its total cash requirements of \$37,341,000 for years 2004 through 2008. The requested \$15 million debt issue is necessary to help Suburban meet its \$14,943,000 external funds requirements.



Capital Ratios

Suburban's capital ratios as of September 30, 2003, are presented below as recorded and adjusted to give pro forma effect to the transactions listed below:

	(dollars in thousands)				
	<u>Recorded</u>		<u>Adjustments</u>	<u>Proforma</u>	
Long-term debt	20,200	30.9%	10,800	31,000	39.5%
Short-term debt	<u>4,000</u>	<u>6.1%</u>	<u>-</u>	<u>0</u>	<u>0.0%</u>
Total Debt	24,200	37.0%	10,800	31,000	39.5%
Preferred Stock	3,982	6.1%	-	3,982	5.1%
Common Equity	<u>37,288</u>	<u>56.9%</u>	<u>6,152</u>	<u>43,440</u>	<u>55.4%</u>
Total Equity	41,270	63.0%	6,152	47,422	60.5%
Total Capitalization	<u>65,470</u>	<u>100.0%</u>	<u>16,952</u>	<u>78,422</u>	<u>100.0%</u>

## Explanation of Adjustments:

a) Debt Securities

1. The issue of Series D Bonds in the amount of \$15,000,000 authorized by this Decision.
2. The projected retirement of \$900,000 long-term debt.
3. The planned refinancing of \$3,300,000 First Mortgage Bonds, Series A issued under D.86-11-013.
4. The decrease of \$4,000,000 in short-term debt.
5. The net of these adjustments is a \$10,800,000 increase in debt.

b) Equity Securities

1. The projected retained earnings of \$6,152,000.
2. The net of this adjustment is a \$6,152,000 increase in equity.

Suburban's authorized capital structure for Test Year 2003, as shown in D.03-05-078 dated May 22, 2003, consists of 37.9% long-term debt, 6.5% preferred equity, and 55.6% common equity.

Capital structures are normally subject to review in cost of capital or general rate case proceedings. We will not, therefore, make a finding in this decision of the reasonableness of the projected capital ratios for ratemaking purposes.

In Resolution (Res.) ALJ 176-3129 dated February 26, 2004, the Commission preliminarily categorized this Application as ratesetting, and preliminarily determined that hearings were not necessary. No protests have been received. Given these developments, a public hearing is not necessary, and there is no need to alter the preliminary determinations made in Res. ALJ 176-3129.

### **Comments on Draft Decision**

This is an uncontested matter in which the decision grants the relief requested. Accordingly, pursuant to Pub. Util. Code 311(g)(2), the otherwise applicable 30-day period for public review and comment is being waived.

### **Assignment of Proceeding**

Izetta C.R. Jackson is the assigned Examiner in this proceeding.

### **Findings of Fact**

1. Suburban, a California corporation, is a water utility subject to the jurisdiction of this Commission.

2. Suburban needs external funds for the purposes set forth in the Application.

3. The money, property, or labor to be procured or paid for by the proposed debt issue is reasonably required for the purposes specified in the Application.

4. Authorizing Suburban to offer, issue and deliver the Series D Bonds with interest rates based on existing market conditions at the time of negotiating the terms as set forth in the Application would not be adverse to the public interest.

5. Authorizing SDG&E to encumber utility assets in the event that such encumbrance will be required to secure the debt issue is for proper purposes and is not adverse to the public interest.

6. Res. No. F-616 specifically exempts debt issues of \$20,000,000 or less from the Competitive Bidding Rule.

7. Pub. Util. Code § 818 requires Commission authorization for the issue of stocks, bonds, notes, or other evidences of indebtedness payable at periods of more than 12 months.

8. The reasonableness of any resulting interest rate and cost of money arising from debt capital is normally subject to review in cost of capital or general rate case proceedings.

9. Suburban has paid the fee of \$11,850<sup>6</sup> required by Pub. Util. Code § 1904(b).

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<sup>6</sup> The amount subject to the fee is \$11,700,000 (\$15,000,000 less \$3,300,000 proceeds to be used to refinance long-term debt authorized by D.86-11-013, whereby the fee of \$8,815 was previously paid for). The fee is determined as follows:  $(\$2 \times (1,000,000/1,000)) + (\$1 \times (9,000,000/1000)) + (\$0.50 \times (1,700,000/1,000)) = \$11,850$ .

10. Notice of the filing of the Application appeared on the Commission's Daily Calendar of February 23, 2004. There is no known opposition to this Application, and the authority requested should be granted.

### **Conclusions of Law**

1. A public hearing is not necessary.
2. The Application should be granted to the extent set forth in the order that follows.
3. This authorization is not a finding of the value of Suburban's stock or property, nor does it indicate approval of matters subject to review in ratemaking proceedings.
4. Suburban is exempt from the Competitive Bidding Rule because the proposed debt issue does not exceed \$20,000,000.
5. Pub. Util. Code 1904(b) provides that no fee need be paid on such portion of any such issue as may be used to guarantee, take over, refund, discharge, or retire any stock, bond, note or other evidence of indebtedness on which a fee has already been paid to the Commission.
6. The following order should be effective on the date of signature.

**ORDER**

**IT IS ORDERED** that:

1. On or after the effective date of this order, Suburban Water Systems (Suburban), upon terms and conditions substantially consistent with those set forth or contemplated in Application 04-02-012 (Application), is authorized to:
  - a) Issue, sell, and deliver for cash up to \$15,000,000 aggregate principal amount of its Series D First Mortgage Bonds (Series D Bonds) due 2024;
  - b) Execute and deliver any and all related documents required for the completion of the proposed financing, including, without limitation, the Fourth Amendment and Supplement of its existing Indenture of Mortgage and Deed of Trust and the proposed Bond Purchase Agreement; and
  - c) Encumber its assets in connection with the debt issue.
2. Suburban shall apply the proceeds of the Series D Bonds authorized for the purposes specified in their Application and discussed in this Decision.
3. Suburban shall file with the Audit and Compliance Branch of the Water Division, copies of the agreements for the sale of the Series D Bonds and the final Fourth Supplemental Indenture within thirty days of the execution of these documents.
4. Suburban's proposed issuance and sale of Series D Bonds is exempted from the requirements of the Commission's Competitive Bidding Rule.

5. On or before the 25<sup>th</sup> day of each month, Suburban shall file the reports required by General Order Series 24.

6. Application 04-02-012 is closed.

This order is effective today.

Dated \_\_\_\_\_, at San Francisco, California.